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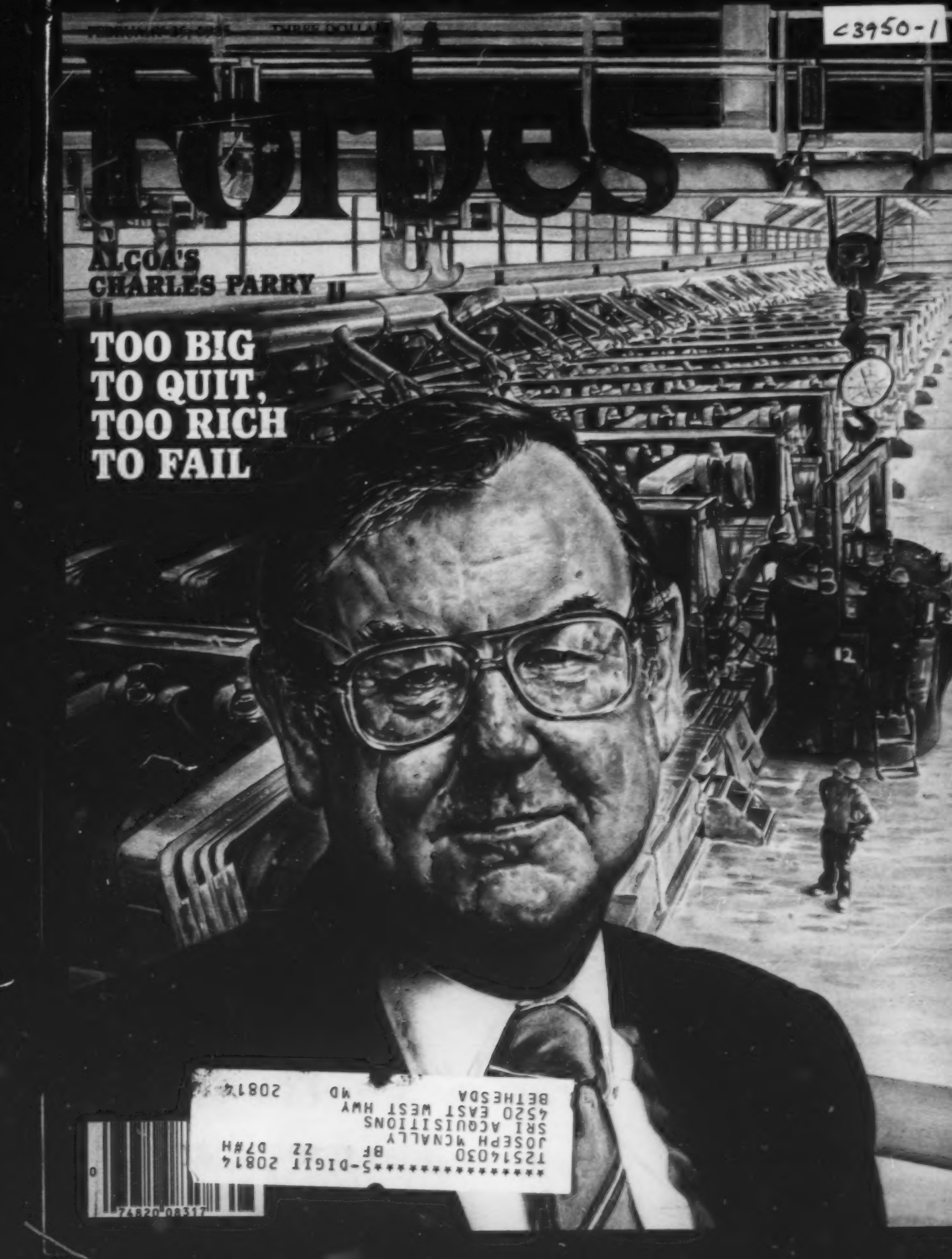
Forbes

ALCOA'S CHARLES PARRY II

# TOO BIG TO QUIT, TOO RICH TO FAIL



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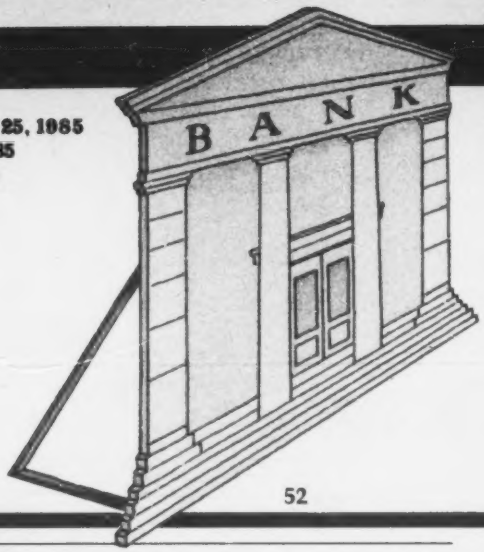


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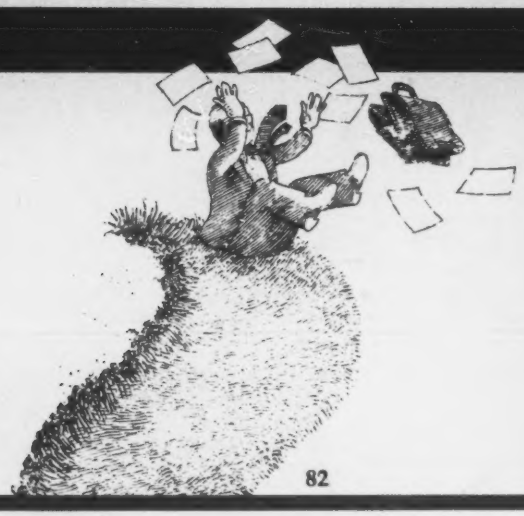

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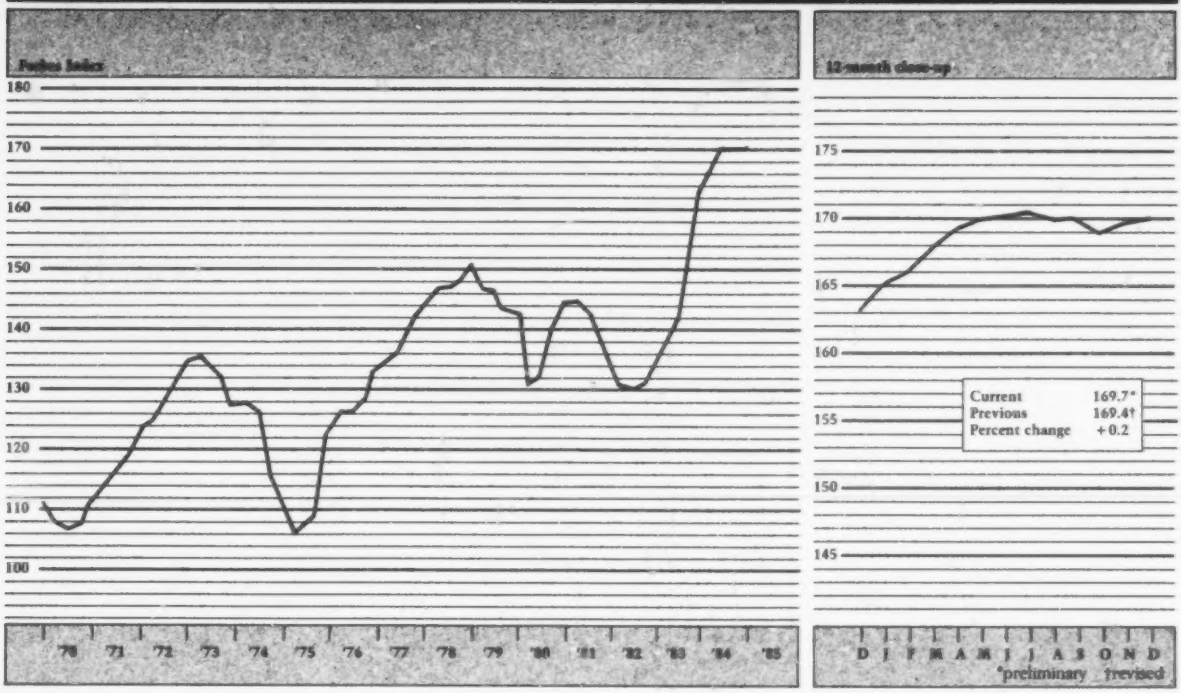
**Cover illustration: Bradford Brown**

# The Forbes Index

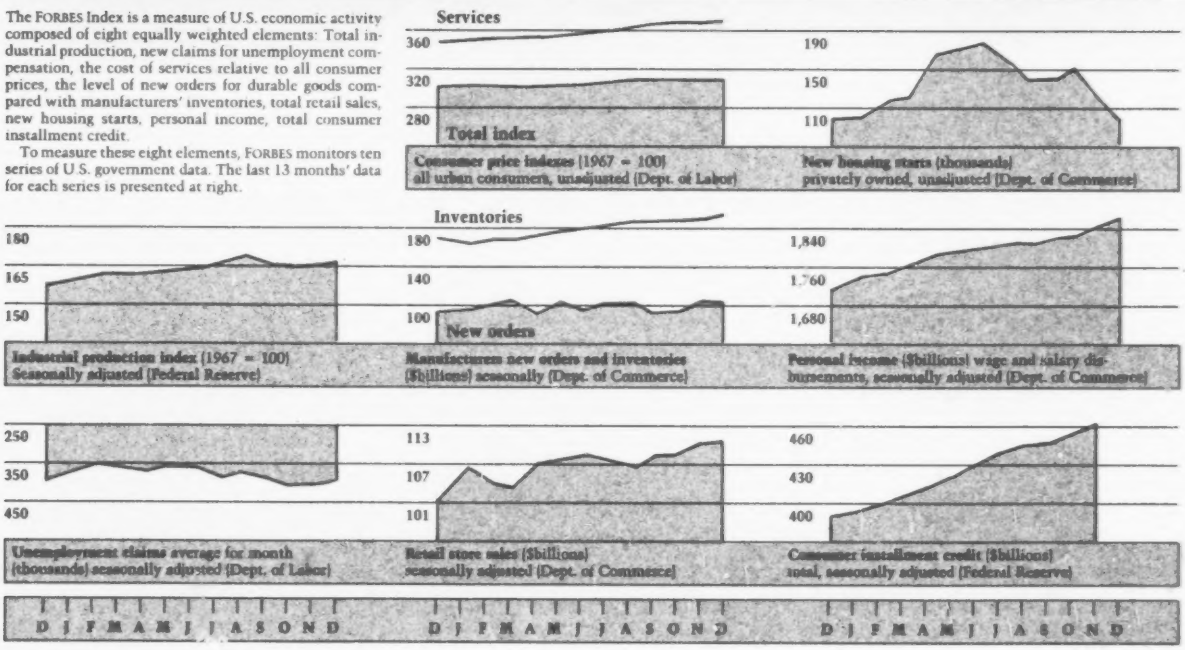



**An uptick, but barely.** Uneven performance in several components held the Forbes Index to a gain of only 0.2%. New unemployment claims decreased 2% from the previous month. The news on inflation was also encouraging. The Consumer Price Index rose less than 0.1% in December, and for all of 1984 it was up only 4%. The services component of the CPI, which includes such expensive items as hospital care, was not quite as tame. It showed a 5.4% gain for the year. Nevertheless, recent inflation levels continue to be significantly lower than they were during the late 1970s and early 1980s. Meanwhile, manufacturers' new orders were off 2.9% from the previous month, but inventories rose 0.4%. And new housing starts were 21.6% lower than they were one month earlier.

## The Forbes Index Components

The FORBES Index is a measure of U.S. economic activity composed of eight equally weighted elements: Total industrial production, new claims for unemployment compensation, the cost of services relative to all consumer prices, the level of new orders for durable goods compared with manufacturers' inventories, total retail sales, new housing starts, personal income, total consumer installment credit.

To measure these eight elements, FORBES monitors ten series of U.S. government data. The last 13 months' data for each series is presented at right.



*There are institutions that look and sound like banks and promise depositors high interest and safety. But some promises are always too good to be true.*

# As good as their word

**By Barry Stavro**

A FEW WEEKS AGO *60 Minutes*, the TV show, told the tragic tale of the depositors of the Commonwealth Savings Co., Nebraska's largest industrial loan and investment company. It failed in November 1983. The 6,700 depositors had $58 million in what they thought were insured accounts, up to $30,000 each. They thought it was a bank, and in most ways but name and legal definition, it was. Banks are supposed to be insured. But Commonwealth's insurance fund failed, too, and those depositors are still waiting to get their first dollar back.

*60 Minutes* did a solid piece on the nastiness in Nebraska, but the problem is bigger than this one bank. Eighteen states have these no-bank banks, for lack of a better term. Sometimes they are called industrial banks or industrial loan companies. Whatever the name, they usually offer tempting interest rates, have about $4 billion in deposits that aren't federally insured by either the FDIC or FSLIC and, as too many depositors are learning—the hard way—too many industrial banks too often go bust.

FORBES counts 13 that have failed or filed for bankruptcy in less than three years. They had $363 million in what passes for deposits. So far, depositors have collected $108 million back.

Industrial banks are a holdover from the pre-Depression state banking system, starting off much like small loan finance companies. But in recent years major bank holding companies like Citicorp and finance companies like Household International have created them, too.

Most of these no-bank banks don't come under federal regulations, and the state inspectors don't seem particularly eagle-eyed, either. Nimbly exploiting slack statutes and loose language, they may take in various deposits by calling them "thrift certificates" or "investment certificates." Inevitably, to cover the higher interest they offer, they make risky loans—second and third mortgages, say, and signature loans.

That makes for high returns. In Iowa last year the average rate on industrial bank loans was an extraordinary 26%. That's why higher rates to savers are promised.

You might think savers would take those fat rates as a danger sign. On the contrary. A lot of savers think anything that looks like a bank must be a bank, and, after all, aren't all banks insured by the federal government?

Not always. Some industrial banks have no insurance. Others have private insurance, but as recent history shows, all too often it's not enough.

Industrial bankers claim they will explain the differences to customers—if they are asked. "However," says Richard Young, president of Topa Thrift & Loan Association, one of California's bigger ($99 million assets) and more conservative industrial loan companies, "if somebody walks in and says they'd like to open up a $50,000 certificate, our people are not instructed to jump up and down and say, 'Hey, but did you realize that this insurance that we have is not as good as on the federal level?' "

Some industrial banks are failing because inflated real estate loans go bad, some because of stealing. Some cynics even think regulated banks might be setting up industrial banks to funnel off their bad loans. Sure, regular banks are going broke, too, but then most depositors quickly get all their money back.

Back in 1971 a private insurance fund was established in California by member industrial loan companies, and other states followed. Unfortunately, it's often paper insurance and not backed by state guarantees.

## The failures

**These institutions may have looked like banks, and even acted like banks, but they had no federal deposit insurance. Too many depositors learned that, the hard way, after these institutions failed.**

| Institution | State | Date failed | Depositors | Amount "insured" (millions) | Repaid so far (millions) |
|---|---|---|---|---|---|
| Commonwealth Savings | Nebraska | November 1983 | 6,700 | $58.0 | $0.0 |
| Western Community Money Center | California | April 1984 | 12,000 | 93.0 | 22.5 |
| Menoa Finance | Hawaii | February 1983 | 6,900 | 33.9 | 11.3 |
| Great Hawaiian Financial | Hawaii | February 1983 | 2,500 | 6.6 | 2.2 |
| American Securities & Loan | Iowa | August 1984 | 2,800 | 5.0 | 3.0 |
| Murray First Thrift & Loan* | Utah | July 1982 | 16,000 | 47.0 | 47.0 |
| Delta Industrial Bank | Colorado | August 1984 | 352 | 1.4 | 1.4 |
| Gunnison Industrial Bank | Colorado | August 1984 | 1,018 | 2.8 | 2.8 |
| Empire Finance Co of Louisville† | Kentucky | July 1983 | 84 | 2.0 | 0.0 |
| BFC Financial Plan† | Kentucky | April 1984 | 160 | 1.7 | 0.0 |
| Southern Industrial Banking Corp† | Tennessee | March 1983 | 5,500 | 52.0 | 18.0 |
| Republic Financial Corp† | Oklahoma | September 1984 | 1,200 | 23.0 | 0.0 |
| Republic Trust & Savings Co† | Oklahoma | September 1984 | 3,200 | 36.0 | 0.0 |

*The state arranged the sale of Murray's assets to a commercial bank, which agreed to repay depositors.
†Not insured.

When Nebraska's Commonwealth Savings failed, thanks to a spider's web of insider loans and a horrendous portfolio of second and third mortages, its depositors thought they could rely on the Nebraska Depository Institution Guaranty Corp. The NDIGC, it turned out, had only $2 million cash in its deposit insurance kitty, not enough to cover its share of Commonwealth's $58 million, so it went bust, too. Now depositors are facing a sorry 50-cent return per dollar after liquidating Commonwealth Savings' assets.

Similar institutions have failed in eight other states *(see table)* in the past few years. Three states—Kentucky, Tennessee and Oklahoma—had no insurance fund at all. Even in states with insurance, the repayment is just trickling in. Only in Colorado has the insurance fund paid account holders in full up front.

Look at what is happening in California. When the Western Community Money Center, based in Walnut Creek, failed (inflated appraisals on bad real estate loans) last April, with $93 million in "insured" accounts, its 12,000 depositors were covered up to $50,000 per account. But, in fact, the depositors had to wait six months to get about 25 cents on their dollar. More money will have to come from further liquidation of Western's assets. It could take four years to get all their principal back. And forget about lost interest.

But they are lucky. The California Thrift Guaranty Corp., the insurance fund for these industrial loan companies, is left with about $14 million in its kitty, while the insured accounts of its state members total about $1.5 billion. "It's not intended to pay the account holders up front to full dollar value at the point of closure," says Roger Duerksen, executive vice president of the California Association of Thrift & Loan Cos., a trade group. How much would you bet that this was perfectly clear to every customer?

Retirees invested nearly $3 million at Western, attracted by the 1-to-3-point premiums. How did Western, which scooted from $5 million to $120 million assets in just two years, handle questions on insurance? Says Jack Carlson, assistant commissioner of California's Department of Corporations: "They said, 'It's protected by Thrift Guaranty Fund.' When an investor would ask, 'What's Thrift Guaranty?' the company would say, 'That's just like FDIC.' "

In Iowa a failed industrial loan company turned out to own a good percentage of three Colorado banks that were all closed by the FDIC, some Orange Julius franchises in Alabama, a timber company and an auto body shop, says Bill Hawthorne, acting director of Iowa's Financial Institutions Division.

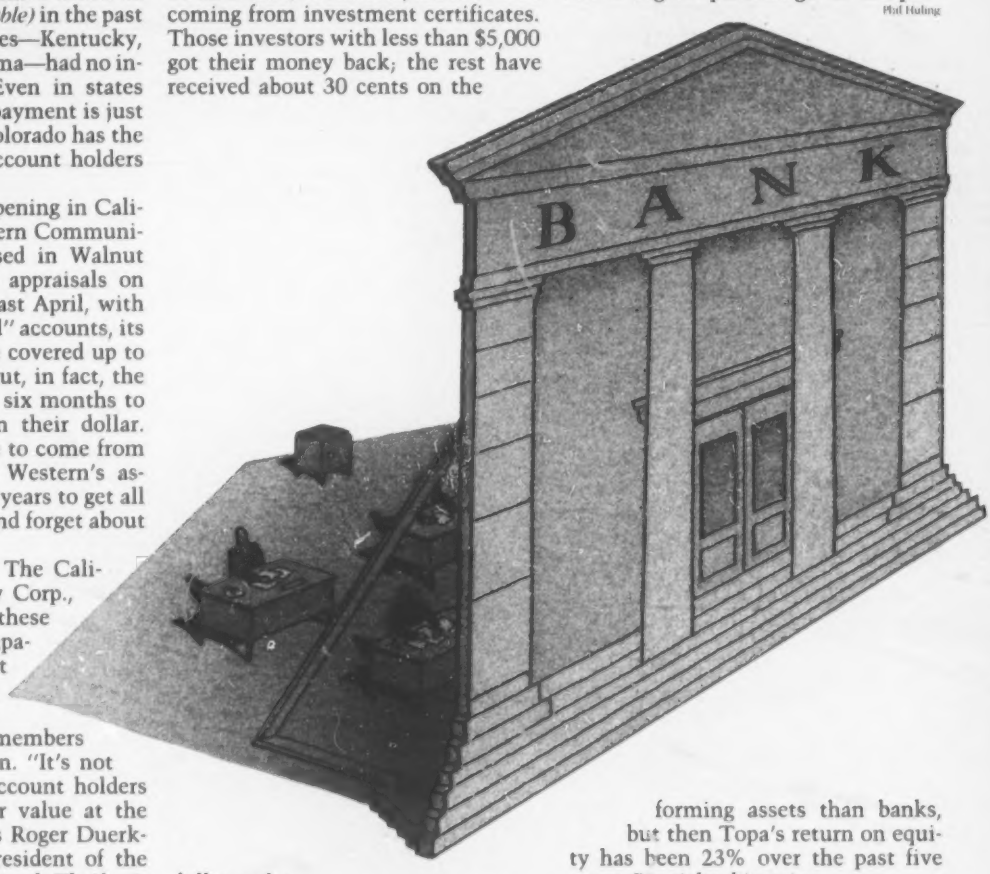
In Tennessee, Jake Butcher's United American Bank of Knoxville was shuttling loans into his brother's Southern Industrial Banking Corp., an industrial loan company. They both went down. Southern's creditors were owed some $52 million, most of that coming from investment certificates. Those investors with less than $5,000 got their money back; the rest have received about 30 cents on the dollar so far.

Industrial banks have been eligible to apply for FDIC insurance since 1982. Most don't want the stricter supervision on their investments and risky loans that come with federal regulation. Of the problem states, only Hawaii has taken action to discipline the industrial banks. Two small industrial loan companies having failed there in 1983 with a total of $40 million in so-called insured accounts (with only $14 million repaid to date), Hawaii now insists that deposit-taking industrial banks must have federal insurance.

In California federal insurance is still only an option. Sixty-five industrial loan companies there, with combined deposits of $1.5 billion, are still privately insured—with that $14 million fund—but nine have FDIC insurance, and others, including Topa Thrift, have applied.

Richard Young of Topa can make a case for these no-bank banks. They often take greater risks and cater to customers who might be self-employed or who need a fast loan decision or who have a shaky credit history—customers that other banks would probably turn down. Yes, Topa has a higher percentage of nonperforming assets than banks, but then Topa's return on equity has been 23% over the past five years. Big risks, big gains.

Phil Huling




"If we became a member of the FDIC system, it might work, but it would change the way we do business," Young says. And he adds: "Because the way we do business is extremely successful, I'm not anxious to change." If the publicity about failing industrial banks grows, he also says, federal insurance would be better than going out of business.

There is a place for those who want to take bigger risks for bigger returns. But only when it's certain, absolutely certain, that every person taking the risk understands it. That doesn't seem true now. ■

*Some cable-TV systems are about to enter a promised land, where costs decline as revenues rise. Others will continue to struggle. Here's how to tell one kind from the other.*

# Fat, wired cats

**By Alex Ben Block**

FOR A BUSINESS that is supposed to be in big trouble, cable television is getting surprisingly strong support in the stock market. An index of 17 leading cable stocks compiled by Paul Kagan Associates of Carmel, Calif. has climbed 37.4% since last May, vs. 13% for the Dow Jones industrials. A handful of operators, notably Adams Russell Co., United Cable Television Corp. and Comcast Corp., have done far better.

What's going on? Paul Kagan, dean of cable-TV analysts, thinks some cable operators are entering a new phase. "Cable systems," he says, "are typically lucrative in the franchising stage, ailing in the construction phase and fat cats when they mature." Many of the country's 6,800 cable systems, Kagan thinks, are now reaching the fat cat stage.

Cable industry revenues for 1984 reached almost $8 billion, according to Bill Daniels & Associates of Denver, with profits before taxes of $800 million. That's up from 1983 revenues of $6 billion and profits of about $400 million. It's a quantum leap from 1982, when Kagan's Sharon Armbrust estimates cable lost around $200 million on revenues of $4.7 billion.

"The leverage in this business is really spectacular," says Daniel L. Ritchie, chairman and chief executive officer of Westinghouse Broadcasting & Cable, which operates Group W

## Wired for profit

**All of these public companies can show strong earnings growth . . . *if* they can add new subscribers. Even with the recent market runup, these companies still trade at a substantial discount from their liquidation values.**

| Cable operator/ parent | Headquarters | Basic subscribers | Homes passed | Penetration rate[1] | Per share[2] earnings | Per share[2] cash flow | Per share[2] long-term debt | Cable as % of parent's revenue | Recent price | Liquidation[3] value |
|---|---|---|---|---|---|---|---|---|---|---|
| Adams Russell Cable<br>Adams Russell Co | Waltham, Mass | 139,102 | 260,000 | 54% | $ 1.28 | $ 3.30 | $ 7.31 | 30% | 26¼ | $ 43 |
| Capital Cities Cable<br>Capital Cities Comm | Bloomfield Hills, Mich | 365,000 | 597,000 | 61 | 10.05 | 15.00 | 16.54 | 9 | 177½ | 253 |
| Comcast Cable Comm<br>Comcast Corp | Bala Cynwyd, Pa | 474,900 | 838,500 | 57 | 0.87 | 2.31 | 7.84 | 85 | 23½ | 38 |
| Cox Cable Comm<br>Cox Comm | Atlanta, Ga | 1,553,305 | 2,735,894 | 57 | 3.09 | 4.17 | 6.40 | 55 | 55⅛ | 107 |
| Heritage Cable<br>Heritage Comm | Des Moines, Iowa | 440,550 | 784,736 | 56 | 0.58 | 3.48 | 10.69 | 44 | 19¾ | 39 |
| Jones Intercable<br>Jones International | Denver, Colo | 431,672 | 700,732 | 62 | 0.30 | 0.67 | 3.52 | 100 | 5 | 11 |
| Multimedia Cablevision<br>Multimedia | Wichita, Kans | 263,708 | 471,000 | 56 | 2.13 | 3.36 | 4.98 | 22 | 43 | 67 |
| Rogers Cable Systems<br>Rogers Cable Systems | Toronto, Canada | 600,000 | 1,100,000 | 55 | –0.86* | 1.13* | 33.76* | 100 | 6⅛ | 11 |
| Scott Cable Comm<br>Scott Cable Comm | Irving, Tex | 55,200 | 79,200 | 70 | 0.58 | 1.38 | 4.49 | 100 | 5½ | 14 |
| Storer Cable Comm Div<br>Storer Comm | Miami, Fla | 1,502,731 | 2,758,622 | 54 | –1.90 | 9.59 | 45.37 | 65 | 51½ | 92 |
| Tele-Comm<br>Tele-Comm Inc (TCI) | Englewood, Colo | 2,766,000 | 5,045,000 | 55 | 0.42 | 22.00 | 2.60 | 100 | 24¾ | 40 |
| Amer TV & Comm Corp<br>Time Inc | Denver, Colo | 2,400,000 | 4,400,000 | 55 | 3.17 | NA | 6.12 | 20E | 48 | 77 |
| Tribune Cable Comm<br>Tribune Co | Mahwah, NJ | 185,000 | 382,000 | 48 | 2.51 | 4.54 | 6.65 | 2 | 35¼ | 67 |
| United Cable TV<br>United Cable TV Corp | Denver, Colo | 759,000 | 1,393,000 | 54 | 0.15 | 1.72 | 15.18 | 100 | 32⅜ | 54 |
| Viacom Cable<br>Viacom International | Pleasanton, Calif | 790,000 | 1,400,000 | 56 | 2.54 | 4.52 | 21.54 | 48 | 38⅛ | 78 |

[1]Percentage of basic cable subscribers among those offered service. [2]For latest 12 months reported. [3]Data from Paul Kagan Associates *Cable TV Investor Newsletter*. * Canadian dollars. E: Estimate. NA: Not available.

## Static in Santa Cruz

A new federal law recently took effect guaranteeing a cable company that its franchise cannot be canceled so long as it provides "reasonable" service. The first serious test of that law, passed after years of lobbying by the cable industry, is now shaping up in Santa Cruz, Calif.

Santa Cruz, 74 miles south of San Francisco, has a 12-channel system built in 1955-56 to overcome reception problems caused by the Santa Cruz Mountains. When Westinghouse's Group W bought Teleprompter in 1982, the Santa Cruz franchise came with it. So did a group of local residents angry about the quality of service. Group W offered to invest $20 million to rebuild the 209,000-home franchise, but local officials wanted more. After years of unhappiness, they insisted on strong protection measures to insure service standards. The local officials also proposed that the city and county own the system, which would then be leased back to Group W to operate. Negotiations to renew the franchise broke down completely last fall.

The city and county then played what they thought was the winning card: They threw the franchise open to new bidders. Thanks to the new cable law, however, Westinghouse is not yet out in the cold. In a suit filed against the city and county of Santa Cruz, Group W claims that the law protects the franchise unless and until the courts hold Group W has not provided reasonable service. In the meantime, Group W has begun the first phase of rebuilding the system. Santa Cruz officials say the federal law doesn't apply. But litigation could take years. The city fathers just might prefer to settle with the operators for what they can get now.—**A.B.B.**

Cable. "If you add a customer, your revenue goes up by $20 a month, but costs may only go up $3." By that rule of thumb, if revenues should climb to $19.2 billion by 1990, as Kagan projects, the cash generated by cable operators should be immense—perhaps $10 billion annually.

With such prospects before them, it's no surprise that many cable operators who had been preoccupied in their ailing years with laying wires are now turning their attention to better marketing. There is still plenty of room to grow. In most large urban areas only about 45% of potential customers have signed up. To the extent that salesmen can boost penetration rates, leverage will lift profits even higher.

Congress, too, has made life sweeter for cable TV. Last October it passed a law (effective Dec. 29, 1984) that may protect cable operators from local politicians' particular notions about service *(see box)*. The new law also allows cable operators to raise basic monthly service rates by 5% this year, by 5% next year, and by as much as the market will bear from 1987 onward. Cable, in effect, will become a kind of unregulated monopoly.

This new freedom in pricing the basic service is especially important because it will help offset the public's lukewarm response thus far to the add-on programming services. Cable operators usually split increases in pay-TV programming fees with the program provider—HBO, say. But when the operator raises the basic rate, he keeps it all. "The new law is the greatest windfall ever for cable," says James A. Parsons, vice president and head of entertainment industry lending for Bank of America in Los Angeles. Parsons estimates the new federal legislation instantly added $100 to $150 per subscriber to many cable systems' values, at a time when even relatively small cable systems were selling for $850 per subscriber.

But not all companies are alike. The cable systems growing into fat cats are those already up and running, particularly those in affluent suburban communities or areas with reception problems. In contrast are some recently won franchises in urban areas that are hurting, many badly.

The newer players in the cable game have two problems. First, cable's basic subscribers—currently just over 35 million homes, or 40% of all TV households—are growing at less than expected rates. Second, and more menacing, a goodly number of competitors are now stuck with the extravagant, even wholly unrealistic, promises they made in order to win the right to wire the biggest U.S. cities. Sacramento's city fathers, for example, initially demanded that the franchisee plant 20,000 trees. In a St. Louis area franchise the winning cable company was told to donate either 20% of its stock or $1 million a year to a nonprofit company that then distributed the proceeds to various social services. The city of Miami tried to get a cable company to pay for an annual antidrug campaign. The demand was dropped only after the FCC ruled it exceeded franchise fee limits.

As a result, some franchise winners have yet to find the capital they need to get going. Example: In 1983 Scripps-Howard Broadcasting of Cleveland, Cablevision Systems Development of Woodbury, N.Y. and a group of local investors won the bidding to wire 330,000 homes in Sacramento. Cablevision, which owns a dozen other systems, anticipated raising its share of the total $166 million cost from limited partnerships, as it had successfully done to fund systems on New York's Long Island and elsewhere. But when Cablevision began seeking investors to put up its first payment of $34 million, due this past Dec. 31, it ran into a wall. "It's been almost impossible to raise money by limited partnerships or almost any other route for urban cable," grumbles Charles F. Dolan, 58, general partner of Cablevision, the largest privately owned U.S. cable company. After missing its scheduled payment, Cablevision was cut out of the Sacramento deal. Scripps-Howard is deciding whether to go it alone or seek a partner. Dolan also has run into trouble building Cablevision's Boston franchise.

Another operator with problems is Warner Amex Cable Communications, a partnership between Warner Communications and American Express. It did extremely well in the franchising wars in big cities such as Dallas, Cincinnati and Pittsburgh by promising to build sophisticated two-way cable systems called Qube. Unfortunately, the cost to build in urban areas was higher than expected, and subscriber sign-ups ran well below projections. Warner Amex' income statement began to hemorrhage. So in 1983 the partners brought in Drew Lewis, Ronald Reagan's tough-minded Secretary of Transportation, to turn Warner Amex around. Since then he has fired most of the headquarters staff and farmed out many of their duties to various affiliates. He spun off 34% of the programming side of the operation (for $75 million), which included the successful MTV: Music Television, as a separate public company. Warner Amex currently has 104 cable systems. By the time he's done pruning, in a year or so, Lewis says, it could well be down to 80 or 90 systems. When it does become profitable, he adds, it's likely Warner Amex also will be spun off as a separate

Jayce Reid

*Westinghouse Broadcasting & Cable's Daniel L. Ritchie*
***"The leverage in this business is really spectacular."***

public company.

Who is buying the cable franchises being sold? One of the systems Warner Amex shed was in Pittsburgh. It was sold to Tele-Communications Inc. (TCI), based in Englewood, Colo., the nation's largest cable system operator, for $92 million in cash and notes, or $1,200 per subscriber. Why was TCI willing to pay so much for a troubled franchise? TCI Chairman Robert Magnus says he isn't looking for present earnings but, rather, for a steady buildup of long-term values. Moreover, he says, it was a good fit. TCI already operated most of the suburban and rural franchises around western Pennsylvania, so it was able to save money by "clustering" such services as billing, marketing and customer installations.

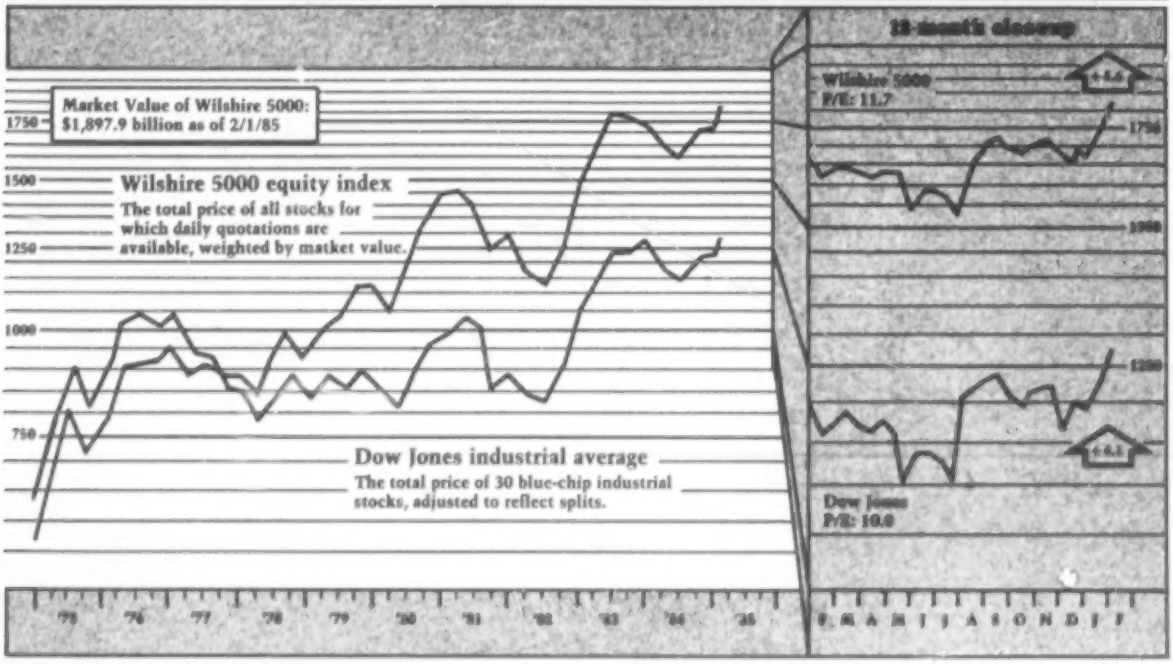
TCI's smartest move, however, has been political. Before buying out Warner Amex, TCI renegotiated the terms of the franchise with Pittsburgh officials, Magnus and TCI's president, John C. Malone, persuading them to let TCI scrap Warner Amex' two-way Qube system, which costs about $1,200 per customer, including sophisticated electronic gear for the headquarters, and substitute a less expensive, one-way system that costs about $120 per subscriber. "You don't get a 747 when you need a 727," says Magnus.

All in all, then, sophisticated investors now see cable as a two-tier industry. Operators in the newer franchises, like Warner Amex and Cablevision, have formidable troubles. But a lot of operators of older systems are entering the promised land of rising revenues, a stable customer base and declining costs. As cable systems' losses turn to profits and then bigger profits, says Denver-based cable analyst and consultant Paul Bortz, "they could become takeover targets."

That, evidently, is what the stock market believes. ■

Edited by Steve Kichen

# The Forbes/Wilshire 5000 Review




**Off to a good start.** With January already history, investors had plenty to smile about. The market continued to show considerable strength as volume remained strong, advancing issues outpaced declining issues and dozens of shares hit 52-week highs. Secondary stocks, on the rebound from their long slump, led the market. During the last two weeks the Amex composite topped major indicators with a 6.1% advance, but the NASDAQ was a close second with a 5.8% gain. Meanwhile, the blue-chip Dow hit its alltime high and flirted with the 1300 level before winding up with a 4.1% increase. The overall market, as measured by the Wilshire index, rose 4.6% during this stretch. Their recent gains notwithstanding, secondary issues still have plenty of ground to make up. The Forbes 500 is ahead 11.7% for the 52-week period, but the NASDAQ and the Amex—with respective gains of 5.4% and 5%—fared less than half as well.

The Wilshire index is some 10.3% higher than it was a year ago; over the recent four-week period the Wilshire gained some $164 billion in total market value. During this time the P/E on the Wilshire jumped from 10.8 to 11.7, an 8% increase. In contrast, the 30-stock Dow industrials are selling at 10 times latest 12-month earnings, while the Forbes 500 sport a multiple of 10.2.

## Close-up On The Equity Markets

**Performance of six leading indexes**

| Percent change | Wilshire 5000 | Forbes 500[1] | Dow Jones industrials | NYSE Composite | Amex Market Value Index | NASDAQ Composite |
|---|---|---|---|---|---|---|
| in last 4 weeks | 9.8 | 9.0 | 7.8 | 9.1 | 10.8 | 13.0 |
| in last 52 weeks | 10.3 | 11.7 | 6.7 | 11.0 | 5.0 | 5.4 |

**Stock performance based on six key investor yardsticks**

| Percent change | Company size | | Volatility[2] | | P/E multiple | | Dividend yield | | Growth profile[3] | | Share price | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | large | small | high | low | over 25 | under 5 | over 7.5% | none | high | low | over $40 | under $4 |
| in last 4 weeks | 9.8 | 14.5 | 13.6 | 7.5 | 14.8 | 9.8 | 6.7 | 16.8 | 13.9 | 8.3 | 8.4 | 16.8 |
| in last 52 weeks | 12.1 | 8.7 | 1.7 | 18.2 | –3.9 | 14.7 | 14.8 | 2.7 | –1.1 | 17.2 | 15.4 | –8.8 |

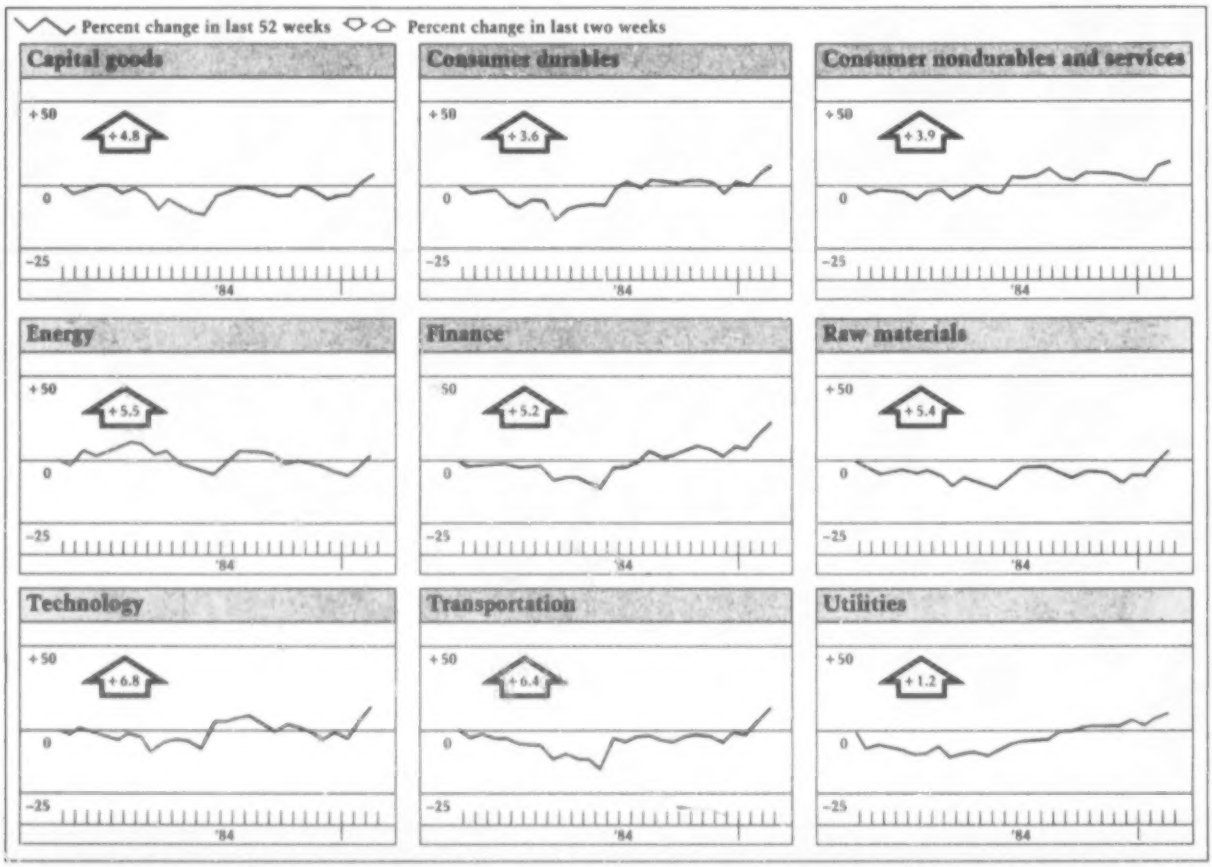
[1]Based on sales.
[2]A stock's sensitivity to overall market movement. High-volatility issues have wide price fluctuations, low-volatility issues are more table.
[3]A quantitative evaluation of a stock's growth image, determined by Wilshire Associates.

Note: All data for periods ending 2/1/85. Prepared by Wilshire Associates, Santa Monica, Calif. Kenneth Alcorn

## Where The Action Is

**High marks for technology.** After months of being battered harder than the other Wilshire sectors, technology stocks appear to have turned the corner. They show the best two- and four-week performance of the lot, with respective gains of 6.8% and 13.9%. Not far behind are transportation shares, which take second-place honors for both the two-week and four-week stretches. Here the railroad and trucking stocks have been strong enough to overcome the recent weakness of airline shares.

During the last two weeks the raw materials and finance sectors posted gains of more than 5%. At the bottom were utility shares, with only a 1.2% increase. These defensive stocks led the market in 1984, but investors now seem willing to take greater risks.




## What The Analysts Think

**A last look at 1984.** Now that the trickle of 1984 earnings reports is turning into a flood, security analysts are making their final adjustments of 1984 earnings projections. In these last few days pessimism continued to reign. Companies in raw materials and consumer durables show the largest cutbacks, utilities the smallest.

**Forecasting the Forbes 500**

| Performance period | Average earnings per share | P/E |
|---|---|---|
| latest 12 months | $3.78 | 10.2 |
| 1984 estimates | 3.89 | 10.0 |
| 1985 estimates | 4.52 | 8.6 |

| Rank based on change in estimate | Sector | Estimated 1984 EPS | Estimated 1984 P/E | % change in 1984 estimate in 2 weeks | % change in 1984 estimate in 4 weeks |
|---|---|---|---|---|---|
| 1 | Utilities | $3.32 | 7.4 | -0.11% | -0.20% |
| 2 | Consumer nondurables | 2.40 | 11.5 | -0.45 | -1.34 |
| 3 | Transportation | 2.60 | 9.6 | -0.55 | -1.90 |
| 4 | Capital Goods | 2.94 | 12.2 | -0.57 | -0.93 |
| 5 | Technology | 2.73 | 11.9 | -0.57 | -1.41 |
| 6 | Energy | 3.72 | 7.8 | -0.71 | -1.07 |
| 7 | Finance | 2.86 | 10.2 | -0.91 | -0.42 |
| 8 | Consumer durables | 4.60 | 8.4 | -1.14 | -1.94 |
| 9 | Raw materials | 2.25 | 10.6 | -1.33 | -2.38 |

Earnings projections are capitalization-weighted consensus estimates from over 2,000 security analysts. Data are compiled and updated continously by the Institutional Brokers Estimate System (IBES), a service of Lynch, Jones & Ryan, a New York-based brokerage firm.

Note: All data for periods ending 2/1/85. Prepared by Wilshire Associates, Santa Monica, Calif.; IBES, a service of Lynch, Jones & Ryan, New York.

*Managers with inside holdings have an extra incentive to work harder for themselves and other stockholders.*

# On insiders' coattails

**By Steve Kichen and Leslie Pittel**

HEFTY PAYCHECKS and cash bonuses are enough to keep many executives working 12-hour days. But when top management also has a sizable equity stake there can be even greater incentives to increase profits and productivity. For starters, if executives are counting on their company stock to get the kids through college, buy the summer house or cover that vacation in the Caribbean, they will work harder to keep its value up. Furthermore, a company that can maintain a high stock price is less susceptible to a hostile takeover.

And later, should a takeover offer come along or management find itself in a position to initiate a takeover, insiders with large shareholdings have a vested interest in bargaining for the highest possible price. In the recent acquisitions of Getty Oil, Prentice-Hall and Gulf, managers and family insiders held out for better offers, benefiting not only themselves but outside shareholders as well.

Then there is the leveraged buyout, a route used by some bosses to enrich their own pockets, avoid public accountability or thwart a hostile acquisition. Canandaigua Wine, Josephson International, Amstar, Dr Pepper, Guardian Industries, Multimedia and Metromedia are among those firms whose managements recently took or are proposing to take their holdings private.

If managers hold a comfortable majority of the shares, they may be less accountable to other shareholders or less likely to receive an overly generous buyout offer. On the other hand, if management owns less than half but attempts a leveraged buyout, even a stingy offer may help outside holders. It could spark off a competing offer, as was the case in the summer of 1983 when Esmark acquired Norton Simon for $35.50 a share, following an initial offer of $29 per share from Norton

## Will management work harder here?

**Insiders hold between 10% and 40% of the outstanding stock of these 37 firms. If they have a selfish interest in boosting share values, that may work to the benefit of outside holders. These issues are reasonably priced, with an average P/E of 10.7, vs. 11.7 for the Wilshire index. The priciest firm sells at a few pennies more than two times book value, while 7 firms sell at or below book value, and none is highly leveraged.**

| Exch | Company | Insider holdings | Recent price | Latest 12-month EPS | P/E | Yield | Current ratio | Book/ share | Debt/ equity | Sales (millions) |
|---|---|---|---|---|---|---|---|---|---|---|
| o | Aceto Chemical | 39% | 25 | $2.42 | 10.3 | — | 3.17 | $17.00 | 14% | $96.4 |
| n | Airborne Freight | 15 | 22¾ | 1.78 | 12.8 | 2.6% | 1.36 | 12.81 | 24 | 334.8 |
| a | Aro Corp | 32 | 30¼ | 3.18 | 9.5 | 4.0 | 6.66 | 23.65 | 15 | 84.2 |
| n | Belding Heminway | 17 | 16⅛ | 1.84 | 8.8 | 2.5 | 2.49 | 15.92 | 20 | 113.6 |
| a | Bundy | 21 | 16½ | 1.04 | 15.5 | 5.2 | 2.20 | 10.86 | 12 | 211.5 |
| o | CPT | 16 | 7⅝ | 0.83 | 9.2 | — | 4.13 | 7.77 | 34 | 200.3 |
| n | Chesapeake Corp of Virginia | 21 | 35¼ | 2.93 | 12.0 | 3.5 | 2.49 | 29.59 | 28 | 273.8 |
| n | Coleman Co | 25 | 29 | 2.82 | 10.3 | 4.1 | 2.48 | 23.28 | 24 | 382.3 |
| n | Commercial Metals | 33 | 17¾ | 1.37 | 13.0 | 2.0 | 2.01 | 19.53 | 27 | 1,170.9 |
| n | Conrac | 18 | 14⅛ | 1.05 | 13.7 | 2.8 | 1.69 | 11.58 | 11 | 141.1 |
| o | Cordis | 14 | 8⅛ | 1.09 | 7.5 | — | 2.96 | 7.57 | 49 | 203.8 |
| a | Cubic Corp | 32 | 20½ | 1.77 | 11.6 | 1.9 | 3.33 | 12.59 | 24 | 273.2 |
| n | Cummins Engine | 16 | 87½ | 19.02 | 4.6 | 2.5 | 1.71 | 53.35 | 45 | 1,604.7 |
| n | Ethyl Corp | 22 | 35⅝ | 3.19 | 11.2 | 2.4 | 2.41 | 19.62 | 49 | 1,745.2 |
| n | Firestone Tire & Rubber | 22 | 18⅛ | 1.69 | 11.2 | 4.2 | 1.57 | 26.66 | 24 | 3,866.0 |

a: American Stock Exchange. n: New York Stock Exchange. o: over-the-counter.

*Sources: CDA Investment Technologies; The Value Line Investment Survey; Standard & Poor's Stockpak-II System, Forbes.*

## Statistical Spotlight

Simon's management.

We decided to put together a list of firms with insider holdings of 10% to 40%. We excluded firms with over 40% insider holdings, figuring that management that already owns close to half of a company is so well entrenched that it need fear no proxy challenge. Since we were seeking companies with potential value that could ultimately be recognized in higher share prices or a takeover offer, we eliminated firms that sell at more than two times book value or have a P/E multiple higher than 16 or a debt-to-equity greater than 85%. We also listed only those firms that have been profitable over the latest 12 months.

But looking for firms with large insider holdings is no simple feat. Duplicate or even triplicate filings that are on record with the SEC, joint holdings, convertible debt and equity, different classes of stock and restricted voting rights accounted for wide discrepancies in published figures on insider holdings. After some culling we ended up with the following list of 37 companies.

With the market on a roll since the start of the year, we were surprised to find as many as seven of our firms selling under book value (although three of this group, CPT, Huffy and Unifi, are priced only a few pennies from book). Firestone Tire & Rubber—the largest firm in the table—shows the steepest discount from its book value. In addition, more than half of the companies on our list have lower multiples than the overall market P/E, which is 11.7 on the Wilshire 5000 index.

When stocks look cheap there is usually a catch. The ones on our list are no exception. Manhattan Industries, for example, has a P/E of 6.9, and for every buck you pay for Manhattan you get almost $1.20 in book value. But this firm is expected to show a loss for the fourth quarter, a result of heavy closeout sales of excess inventories of women's wear.

Jay Meltzer, a textile analyst with Goldman, Sachs, notes, "Manhattan Industries has a low P/E because earnings are coming down. And book value will be eroded by fourth-quarter losses." But Meltzer feels that once this firm balances its inventories with sales it will be able to operate in the black again.

Insiders control only 10% of Planning Research, an engineering and computer services firm, which currently sells near the market multiple. A large NASA contract recently expired, and sales growth could also be dampened by government budget cutbacks. Analysts who contribute to the Institutional Brokers Estimate System are predicting earnings of $1.44 a share for the fiscal year ending this June. That's not as good as the $1.62 the company earned in fiscal 1984 but better than its latest 12-month performance of only $1.22.

Large insider holdings, of course, provide no guarantee that other shareholders will profit handsomely. Owner-managers can drive a firm to bankruptcy about as well as anyone else. In recent years, for example, the likes of Charter Co. and Bobbie Brooks have entered Chapter 11, despite double-digit levels of inside ownership. But when managers have a personal interest at stake, they are likely to work that much harder to make sure that things go right. ■

### Will management work harder here?

| Exch | Company | Insider holdings | Recent price | Latest 12-month EPS | P/E | Yield | Current ratio | Book/ share | Debt/ equity | Sales (millions) |
|---|---|---|---|---|---|---|---|---|---|---|
| o | Flexsteel Inds | 22% | 15½ | $1.61 | 9.6 | 3.1% | 4.91 | $ 9.61 | 15% | $130.5 |
| n | General Housewares | 12 | 10¾ | 0.87 | 12.4 | 2.2 | 2.93 | 12.36 | 30 | 87.0 |
| n | House of Fabrics | 34 | 18¾ | 1.63 | 11.5 | 2.1 | 1.79 | 11.44 | 3 | 239.6 |
| n | Huffy Corp | 15 | 12¼ | 1.58 | 7.8 | 3.3 | 2.64 | 12.29 | 44 | 272.6 |
| n | Kollmorgen | 20 | 21⅛ | 1.41 | 15.2 | 1.5 | 2.78 | 10.62 | 68 | 260.7 |
| n | Leggett & Platt | 27 | 19⅛ | 2.24 | 8.6 | 2.3 | 2.45 | 11.57 | 60 | 364.1 |
| n | Manhattan Inds | 18 | 15¼ | 2.27 | 6.9 | 1.9 | 2.29 | 18.89 | 61 | 433.0 |
| o | MTS Systems | 14 | 17½ | 1.41 | 12.4 | 1.4 | 1.92 | 13.07 | 37 | 74.8 |
| n | National Presto Inds | 16 | 28 | 2.10 | 13.3 | 3.6 | 8.94 | 20.46 | 4 | 103.6 |
| n | Outboard Marine | 12 | 27 | 3.02 | 8.9 | 2.4 | 2.57 | 21.35 | 25 | 921.6 |
| o | Oxford Inds | 40 | 13⅜ | 1.92 | 7.0 | 3.0 | 1.88 | 10.89 | 17 | 577.3 |
| n | Planning Research | 10 | 13½ | 1.22 | 11.1 | 1.5 | 1.54 | 8.18 | 30 | 319.5 |
| o | Service Merchandise | 10 | 12⅞ | 1.47 | 8.8 | 0.6 | 1.38 | 8.55 | 52 | 1,458.1 |
| n | Southdown | 31 | 45¼ | 4.16 | 10.9 | 1.1 | 1.33 | 27.97 | 82 | 237.7 |
| n | Stop & Shop Cos | 23 | 43⅜ | 4.52 | 9.6 | 2.3 | 1.63 | 25.45 | 54 | 2,790.8 |
| n | Tektronix | 19 | 65½ | 6.84 | 9.6 | 1.5 | 3.22 | 39.56 | 12 | 1,331.3 |
| n | Thomas Inds | 25 | 17⅞ | 1.83 | 9.8 | 3.8 | 3.82 | 8.80 | 59 | 222.0 |
| a | Tultex | 17 | 13¾ | 1.06 | 13.0 | 3.2 | 1.92 | 8.24 | 69 | 288.0 |
| o | Unifi | 14 | 10⅛ | 0.68 | 14.9 | — | 2.94 | 10.39 | 27 | 216.5 |
| n | US Shoe | 10 | 28⅛ | 1.96 | 14.3 | 3.1 | 1.74 | 17.12 | 11 | 1,507.8 |
| o | Willamette Inds | 22 | 40 | 3.17 | 12.6 | 3.8 | 1.40 | 28.08 | 48 | 1,045.7 |
| n | Wynns International | 22 | 20⅜ | 2.69 | 7.6 | 2.9 | 3.04 | 15.93 | 18 | 188.0 |

a: American Stock Exchange. n: New York Stock Exchange. o: over-the-counter.

*Sources: CDA Investment Technologies; The Value Line Investment Survey; Standard & Poor's Stockpak-II System; Forbes.*